



Oklahoma Economic Report™

News and analysis of Oklahoma's economy

A publication of the Office of the State Treasurer • Treasurer Ken Miller, Ph.D.

Covering your assets

A recent legislative study revealed for the first time a snapshot of the state's vast real estate holdings, and the image both surprised and concerned the panel's members. The tally of more than 9,000 state-owned properties and buildings, while the most thorough accounting to date, lacks significant details about each parcel's condition and value. Policymakers are trying to accurately determine state property ownership and don't yet have a complete answer.

It's a familiar problem for those leading Oklahoma's government modernization movement. Assessments of the state's fleet of vehicles, purchasing

procedures, information technology infrastructure, and now real estate, have found a decentralized, inefficient, and unaccountable process for managing state assets.

To policymakers' credit, the revelations have generated swift reform efforts. There is now a full accounting of all state owned vehicles and uniform procedures governing their use; purchasing has evolved to a centralized and largely electronic process; and an outdated and fragmented technology infrastructure is being updated so that agencies' systems will work in sync with the rest of the state.

While these reforms are moving the state in the right direction, there is still a lot that needs to be done to ensure better use of the state's resources.

John Morrison, Administrator for the Department of Central Services, is working to fill in the details of state-owned properties. He began building the agency's property database from scratch in 2005 with file cabinets full of handwritten deeds and papers.

Morrison said the state has historically made real estate decisions one parcel at a time. The absence of any master plan for state facilities has led to the current piecemeal and scattered state holdings that exist today. Successful

SEE ASSETS PAGE 3

Inside

- Treasurer's commentary: Rhetoric versus reality: Incentives
- Oklahoma economy rises
- Gross receipts and general revenue compared
- Economic Indicators

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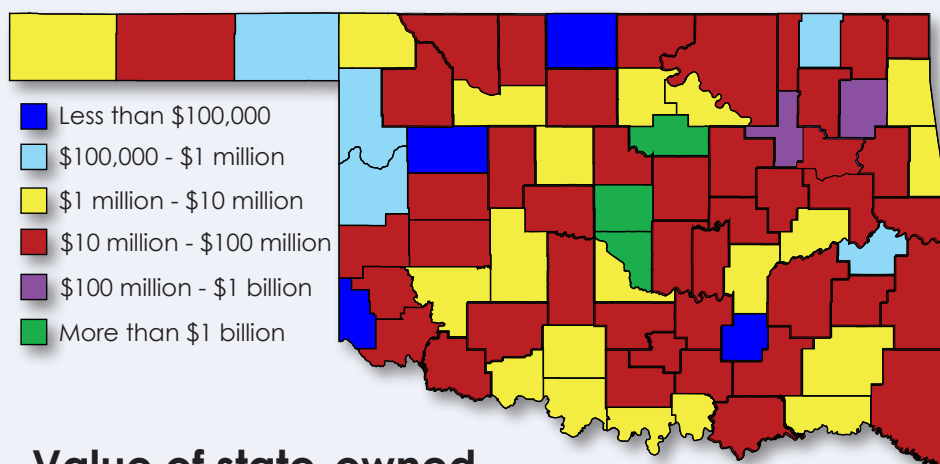
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Government-owned buildings



Value of state-owned buildings by county

Source: Department of Central Services



Treasurer's Commentary By Ken Miller, Ph.D.



Rhetoric versus reality: Incentives

Critics contend that if politicians are good at anything, it is studying something to death. While this legislative interim has been full of task forces and studies, many promise to be more than just simple academic exercises. True, some are meant to garner attention for a favored issue. Others are meant to bolster an opinion. And some are honest undertakings in search of good policy.

And there are some with elements of each of the above. Facing a December 31 report deadline, the Task Force for the Study of Tax Credits and Economic Incentives is preparing final recommendations.

It is this task force member's hope that rhetoric and ideology will play a subordinate role to sound policy and economic reality. The task force recommendations can impact our business climate for years to come and must take into account the competitiveness of states in attracting industry and economic growth.

There is unanimity among task force members that all incentives should meet the three-way test of public purpose, consideration and controls. The panel has concluded the state grants too many tax incentives, many of which need to expire, and that

all incentives need stricter controls, accountability and sunset dates.

There is no such unanimity on the issue of transferable tax credits, which can be sold to a third party when the original recipient does not earn enough taxable income. Only one other state, Iowa, has recently considered eliminating tax credit transferability. The recommendation, made by a similar task force, was not adopted by its Legislature.

“ . . . the criteria should boil down to a cost-versus-benefit analysis.”

As with all incentives, the criteria should boil down to a cost-versus-benefit analysis. If our Legislature determines that an economic benefit, like infrastructure improvement or job creation, is worth a predetermined cost in tax revenue, it is difficult to understand in concept why it matters which company claims the tax credit after the three-way test has been met and the induced benefit received by the state.

It has been argued that it matters

because among the largest purchasers of tax credits is the insurance industry, whose remittances are earmarked for pension funding. However, such logic is just as flawed as saying that the state income tax rate cannot be lowered because its remittances are earmarked for education. Also perplexing is why the secondary market for credits has been met with demagoguery by those who usually favor mutually beneficial voluntary exchange.

Although no new transferable tax credits have been granted in the last seven years, certainly there were poorly structured ones allowed in the past. But there have been beneficial ones as well. Facts fail to confirm the claim that all transferable tax credits, regardless of structure, are inherently bad. Everyone is entitled to their own opinion, but not their own facts and it is the latter that is currently missing from an informed decision.

Another area of divergent thought relates to accountability. Some

SEE COMMENTARY PAGE 3



Commentary

FROM PAGE 2

task force members want the State Auditor's powers expanded to judge an incentive's worthiness.

Others are not yet convinced the case to grow government and spending has been made, or if it is even an appropriate use of the Auditor's office. The Tax Commission seems the more appropriate agency for such determination and is already auditing most incentives.

Further, if three-year sunset provisions are implemented, it seems wasteful for taxpayers to fund additional annual or biannual audits on expiring incentives. Facing sunset, the beneficiary will have to make the case for extension to legislators who stake their reputation with each push of a button.

Should it be determined existing audits are not enough, the panel should consider having tax credit beneficiaries pay the cost of outside independent audits. It bears remembering the courts provide the ultimate remedy for violations of the constitution and public trust.

Like those that have gone before it, this interim has seen its share of studies with varying degrees of worth. With well thought-out recommendations and proper legislative follow-through, the incentive task force will help breathe new life into job-creating tax reform, better budget prioritization and a stronger Oklahoma economy.

Assets

FROM PAGE 1

property management models in both the private and public sectors begin with a centralized place for decision making, something Oklahoma state government currently lacks, Morrison said.

Without a single entity to handle project requests or to prioritize needs and funding, agencies annually come to the Legislature and other bond-issuing authorities seeking approval for new facilities.

Often this results in facilities that don't adequately meet needs. "The agencies aren't building professionals," said Morrison, who contends that agencies should be free to focus on their core missions and leave physical plant decisions to the professionals.

Morrison said the state would be better equipped to determine and meet an agency's facility requirements if it implemented a master plan, similar to how transportation officials prioritize road and bridge projects and maintenance.

Only after there is a proper accounting of each property and an assessment of its functionality can the proper authorities begin effectively meeting agency needs. Buildings deemed unusable by the state should be offered for sale.

While past government reform efforts are yielding savings and efficiencies, this latest focus presents a new opportunity for the state: the chance to reduce dependence on taxpayer funds and bond debt.

Just as important as executing an effective property management program

is deciding the best use of resulting revenue. Many states that have sold off unnecessary assets have done so to help solve immediate budget woes. But Oklahoma's approach should be for the long-term benefit of the state and not a "dash for cash," according to State Treasurer Ken Miller.

Miller believes proceeds should first be placed in a fund dedicated to maintaining state buildings. "We're not taking care of the buildings we have," he said, noting the State Capitol needs approximately \$130 million in repairs.

“ . . . no new state-funded construction should be approved until there is a commitment to take care of existing facilities.”

Miller said one-time revenue exceeding maintenance needs should be used to pay down state debt. He also advocates that no new state-funded construction should be approved until there is a commitment to take care of existing facilities.

Most states do not have a dedicated purpose for revenue from asset sales. For example, in New Jersey, where the state treasurer disposes of state surplus real estate through the Property Management Services division, proceeds

SEE ASSETS PAGE 4



October gross receipts & General Revenue Fund

A comparison of the Treasurer's November 3 Revenue Report and State Finance's November 15 General Revenue Fund (GRF) allocation report illustrates key differences.

October gross receipts totaled \$838.01 million, while the GRF received \$408.1 million or 48.7 percent of the total. Last month, the GRF received 54.8 percent of the gross.

The differences are due to variances in the transfer of funds for rebates and dedicated funding.

In October, the GRF received:

- 64.4 percent of personal income tax
- 41.9 percent of corporate income tax
- 45.3 percent of sales tax receipts
- 69.7 percent of the gross production (GP) tax on natural gas
- 22.8 percent of GP oil tax revenue.
- 32.8 percent of motor vehicle tax collections
- 36.6 percent of other revenue sources

GRF collections for the month topped the estimate by \$24.3 million or 6.3 percent.

Tribal gaming fees generated \$10.2 million during the month.

Insurance premium taxes totaled \$179,000 in October.

Oklahoma economy rises above worldwide chaos

In spite of external threats, volatile markets and global instability, Oklahoma's economy is rising above the chaos, State Treasurer Ken Miller said as he released the state's monthly gross receipts report.

"With yet another month of healthy collections, it appears Oklahoma's economy is hitting its stride," Miller said.

October collections were 7.4 percent higher than in October of last year, showing steady improvement in the state's economy.

Collections over the past 12 months are up almost nine percent from the previous 12 months.

Miller said gross revenue, a reflection of the state's economic performance, has grown for 20 consecutive months.

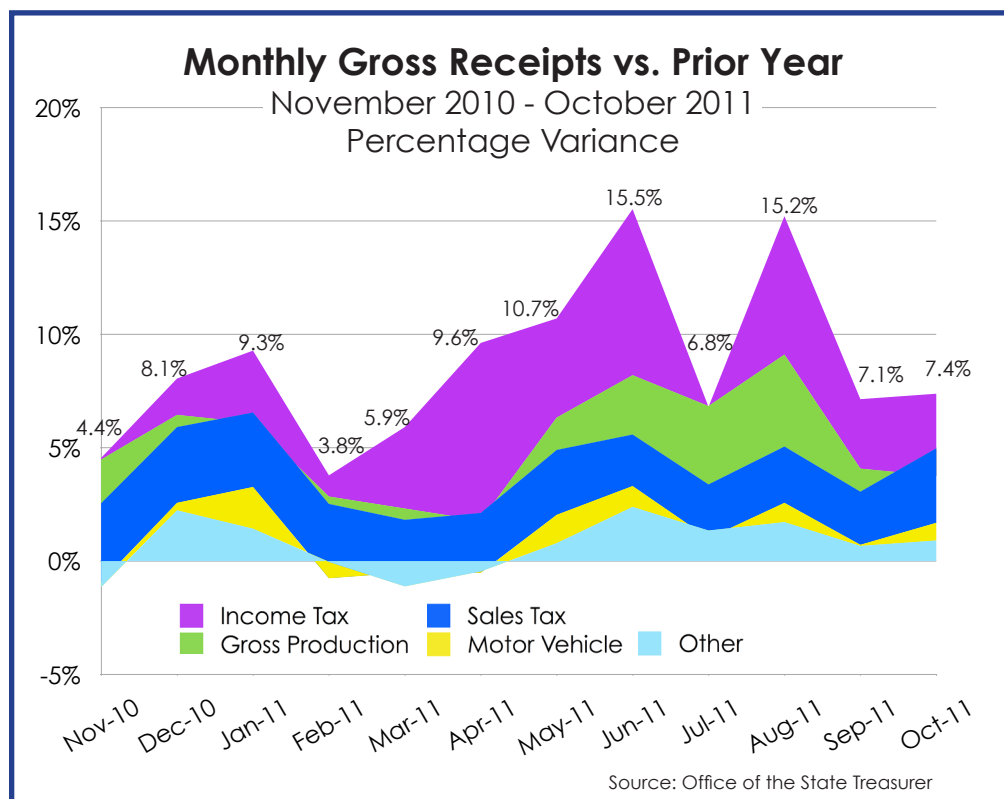
"We have regained almost 60 percent of the revenue that disappeared during the recession," he said.

"We saw a more than \$1.9 billion drop in 12-month receipts between December 2008 and February 2010. Since then, we have seen an increase of more than \$1.1 billion."

Oklahoma: A positive example

As world financial markets react to uncertainty in Washington, Europe and the Middle East, Miller said Oklahoma's

SEE REVENUE PAGE 5





Revenue

FROM PAGE 4

economy is setting a positive example.

“Oklahoma’s two major revenue streams, income tax and sales tax, are showing remarkable resilience,” he said.

“Income tax collections – up by almost 12 percent this month – show Oklahomans are making more money, and sales tax collections – up by almost nine percent – show we are also gaining confidence.”

Miller said the latest Business Conditions Index for Oklahoma continues to reflect a positive outlook for the state’s economy. The index for October shows anticipated growth for the next three to six months.

“With yet another month of healthy collections, it appears Oklahoma’s economy is hitting its stride.”

By contrast, the index for a nine-state region of the Midwest and Plains, of which Oklahoma is a member, dipped slightly below the positive benchmark. Oklahoma and North Dakota, both energy-rich states, continue to outperform the other states in the region.

“In spite of record levels of money circulating throughout our economy, core inflation in the region is at its lowest level since the end of the recession,” Miller said.

“Low price levels help both consumers and policymakers as we work our way back to fiscal health.”

The nine-state region includes Arkansas, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota and Oklahoma.

Assets

FROM PAGE 3

are deposited into the state’s general revenue fund, where they are “re-appropriated” back to the agency which held the property.

When the state is able to generate income from consolidating its assets, lawmakers will have to stand firm against agency pleas to fund ongoing operations with this one-time money. A disciplined approach will be required to preserve the funds for a dedicated purpose such as infrastructure investments or debt reduction.

Leonard Gilroy, Director of Government Reform for the Reason Foundation, urged legislators to not deposit sales revenue into the state’s general fund, a comment that echoed a recommendation from Governor Mary Fallin’s Task Force on Economic Development and Job Creation. This panel contends, “Simply using the proceeds from surplus assets sales or savings from privatization to fund annual operations of state government is not appropriate.”

Some suggest there are other revenue-generating, government-shrinking opportunities beyond paring down the plots of state-owned land and buildings. Long-mentioned by those debating government vs. private responsibility include functions like state-owned power generation facilities, state

insurance providers, turnpikes, water rights and the state lottery.

Asset management, taken as whole, is a commitment to developing a comprehensive, strategic approach for fiscal responsibility, better transparency and accountability, and better planning for state needs.

Policymakers have made notable strides in accounting for state assets and getting the state’s balance sheet in order. For state government to accurately depict its holdings, a thorough accounting of its debts and liabilities should also be a part of the conversation.

A comprehensive and centralized approach for asset and cash management will help prevent the state’s list of properties from unnecessary growth.

As the state works to better define its core responsibilities and develop a long-term plan for asset and cash management, it should incorporate existing state debt and future infrastructure investments.

State jobless rate increases

Figures released November 22, by BLS and the OESC show Oklahoma’s unemployment rate increased to 6.1 percent in October.

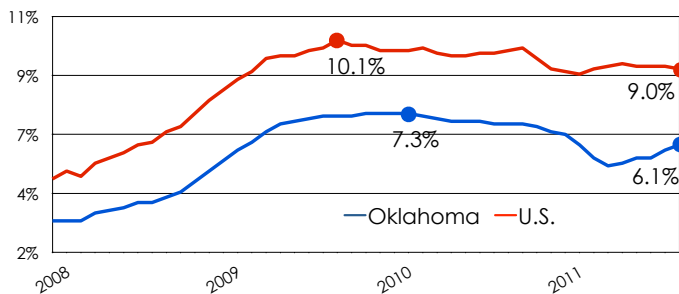
That is 0.2 percentage points higher than the 5.9 percent rate reported in September and compares to 6.9 percent unemployment in October 2010.

The increase is due to labor force growth exceeding employment growth by 3,670. A total of 2,230 jobs were added during the month.



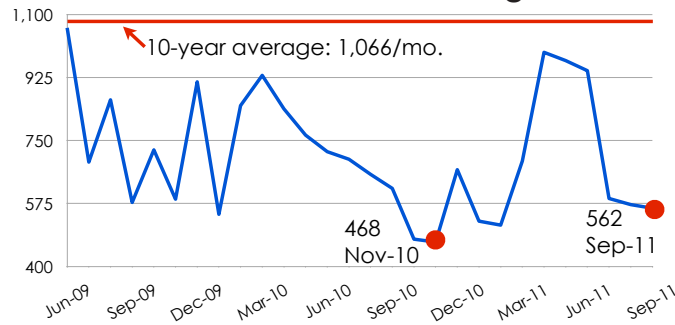
Economic Indicators

Unemployment Rate U.S. vs. Oklahoma



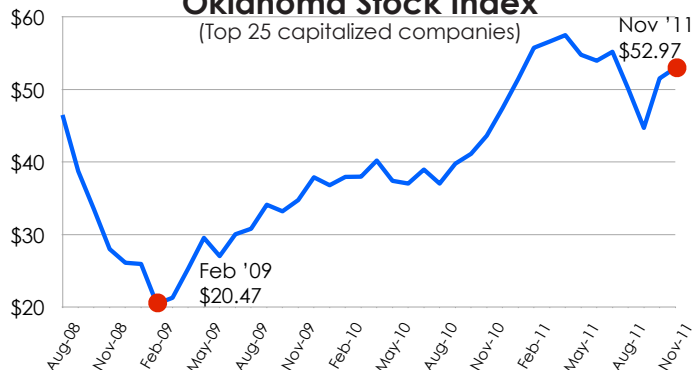
Source: Bureau of Labor Statistics

Oklahoma Residential Building Permits



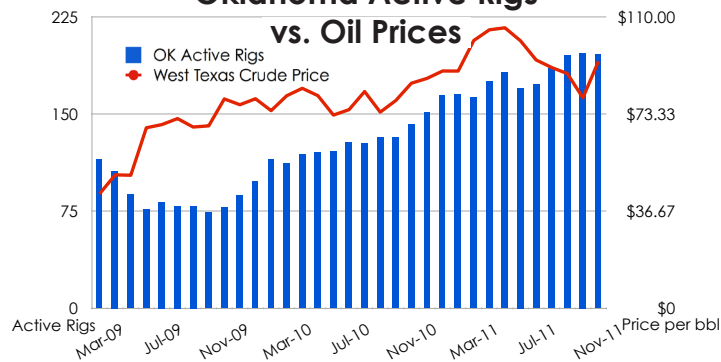
Source: Department of Commerce, Bureau of Census

Oklahoma Stock Index (Top 25 capitalized companies)



Source: Office of the State Treasurer, Budget & Finance Division

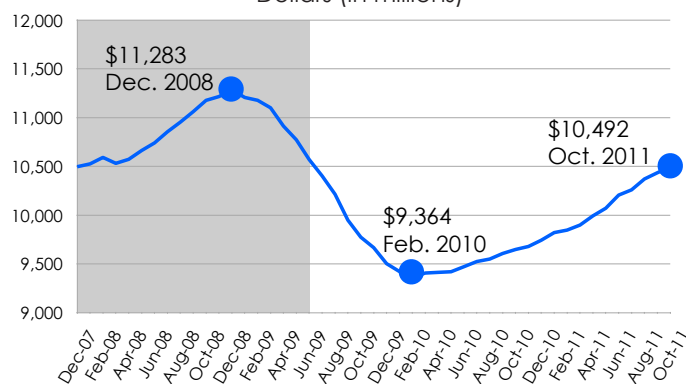
Oklahoma Active Rigs vs. Oil Prices



Source: Baker Hughes & U.S. Energy Information Administration

Oklahoma 12-Month Gross Receipts

December 2007 - October 2011
Dollars (in millions)



Shaded area denotes U.S. recession

Source: Office of the State Treasurer

Interest Rate Forecast

68 Economists

| | 4Q 2011 | 1Q 2012 | 2Q 2012 | 3Q 2012 | 4Q 2012 | 1Q 2013 |
|----------------------------|---------|---------|---------|---------|---------|---------|
| Fed Funds Target | 0.25% | 0.25% | 0.25% | 0.25% | 0.25% | 0.25% |
| 3-M LIBOR | 0.45% | 0.43% | 0.41% | 0.44% | 0.45% | 0.45% |
| Treasury Notes | | | | | | |
| 2-Year | 0.25% | 0.30% | 0.40% | 0.45% | 0.51% | 0.66% |
| 10-Year | 2.10% | 2.20% | 2.40% | 2.55% | 2.70% | 2.85% |
| Treasury Bonds | | | | | | |
| 30-Year | 3.20% | 3.30% | 3.50% | 3.60% | 3.70% | 3.80% |
| Economic Indicators | | | | | | |
| Real GDP | 1.80% | 2.20% | 2.50% | | | |
| Unemployment | 9.00% | 8.80% | 8.30% | | | |

Source: Media forecasts for key economic indicators as surveyed by Bloomberg, November 14, 2011